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November 13, 1978

Letter Report No. 726

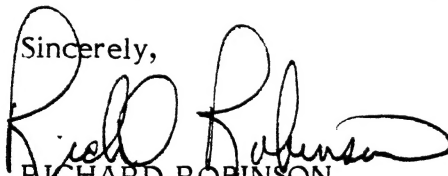
Honorable William Greene, Chairman
Senate Industrial Relations Committee
Room 2183, State Capitol
Sacramento, California 95814

Dear Mr. Chairman:

The Joint Legislative Audit Committee forwards the Auditor General's letter report on the State's Liability for Workers' Compensation.

The auditors are Harold L. Turner, Audit Manager; Mimi Quiett; Gerald A. Silva and Michael L. McGarity.

Sincerely,


RICHARD ROBINSON
Chairman



Joint Legislative Audit Committee

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November 8, 1978

Letter Report No. 726

Honorable Richard Robinson
Chairman, and Members of the
Joint Legislative Audit Committee
Room 4149, State Capitol
Sacramento, California 95814

Dear Mr. Chairman and Members:

In response to a resolution of the Joint Legislative Audit Committee, we have determined that the State's total estimated outstanding liability for workers' compensation for injured and disabled state employees, exclusive of certain law enforcement employees, is \$127 million. This liability exists because most state agencies are legally uninsured; that is, they pay workers' compensation benefits as they are due, rather than cover the liability through an insurance policy. This study was conducted under the authority vested in the Auditor General by Section 10527 of the Government Code.

BACKGROUND

Workers' compensation is a legislatively established, no-fault insurance system which provides compensation benefits to and pays medical expenses for employees who are injured or disabled in the course of employment. Virtually every employee in the State is covered under the workers' compensation laws. Employers are classified as either insured, self-insured or legally uninsured. Insured employers purchase an insurance policy which covers their liability. A self-insured entity is required to post a bond or securities with the Department of Industrial Relations to assure its ability to pay the benefits. Legally uninsured entities include state agencies, city and county governments, etc., which are not required to make advance provision for the liability, but rather pay benefits as they are due.

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Liability for Potentially Re-opened Cases

A liability also exists for cases that have been closed but might re-open. We estimated the liability based on the re-opened claims history for state cases during 1977.

Adjustment and Administrative Costs

The State's liability also includes claims adjustment and administrative costs.

THE STATE'S ESTIMATED OUTSTANDING LIABILITY FOR WORKERS' COMPENSATION

Including all aspects of the liability as discussed above, the outstanding workers' compensation liability of state agencies that are legally uninsured is \$127 million, exclusive of coverage for certain law enforcement employees. This liability exists because most state agencies are legally uninsured; that is, they pay workers' compensation benefits as they are due, rather than cover the liability through an insurance policy.

Some agencies purchase a policy to cover all or some of their employees. Five to 10 percent of state employees are covered this way, and the annual premium cost for this coverage in fiscal year 1976-77 was approximately \$2 million. SCIF is responsible for the entire liability for compensation and medical benefits for employees so covered.

For agencies that elect to be legally uninsured, SCIF provides claims adjustment services under a contract with the Department of General Services. SCIF pays all medical expenses and compensation benefits, then bills the state agencies for the amount paid plus a fee for services. As a legally uninsured employer, the State is responsible for the entire liability.

Benefits in Lieu of Workers' Compensation

There are two types of special salary continuation benefits which certain state employees may elect in lieu of workers' compensation. These benefits are Industrial Disability Leave (IDL), available to members of the Public Employees Retirement System and the State Teachers' Retirement System, and "4800 time" (described in Section 4800 of the Labor Code), available to certain California Highway Patrol and Department of Justice employees. SCIF adjusts the claims and verifies the disability to the agency.

For most eligible employees, IDL benefits are greater than regular workers' compensation benefits. IDL benefits are paid by the State Controller's Office and are accounted for under the agency's staff benefits budget.

The law enforcement employees eligible for "4800 time" benefits receive full salary for up to one year for work-related injuries. The departments pay "4800 time" benefits out of their salary budget. No estimates of the outstanding liabilities are available for "4800 time" compensation; however, California Highway Patrol payments for "4800 time" benefits have been about \$2 million annually and the Department of Justice reported costs of about \$125,000 for 1977.

Table 1 presents the estimated outstanding liability for workers' compensation for state employees, exclusive of "4800 time" benefits.

TABLE 1
*** UNAUDITED ***
WORKERS' COMPENSATION:
ESTIMATED OUTSTANDING LIABILITY*
AS OF DECEMBER 31, 1977
FOR STATE EMPLOYEES
EXCLUSIVE OF CERTAIN LAW ENFORCEMENT EMPLOYEES

	<u>Regular</u>	<u>IDL</u>
All open reported cases	\$ 91,700,000	\$ 400,000
IBNR: projection based on 1977 reporting	10,100,000	1,400,000
Re-opened: projection based on 1977 reporting	<u>7,400,000</u>	
Subtotal	<u>\$109,200,000</u>	
Administrative costs	<u>\$ 16,400,000**</u>	<u>**</u>
TOTAL	<u>\$125,600,000</u>	<u>\$1,800,000</u>

* All figures rounded to the nearest \$100,000.

** Amount based on billed total and includes costs of adjustment for both IDL and "4800 time" claims.

*** UNAUDITED ***

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ADDITIONAL LIABILITIES
FOR SPECIAL FUNDS

In addition to the State's liability for its own employees, the State also provides for workers' compensation benefits as specified in a number of special programs, including:

- The Subsequent Injuries Fund
- The Disaster Service Workers' Fund
- The Uninsured Employers Fund
- The In-Home Supportive Services Program.

Subsequent Injuries Fund

The Subsequent Injuries Fund provides an incentive to employers to hire the disabled by providing benefits for certain permanent disabilities which arise from industrial injuries to an employee who has suffered from a previous permanent disability. Certain subsequent injuries, because of their nature, result in a combined disability rating which is greater than the sum of the ratings for each injury considered separately. The employer is not liable for compensation for the combined disability, but only for that portion due to the later injury when considered by itself. The Subsequent Injuries Fund pays the difference between the combined rating and the sum of the individual ratings.

The cost of the program is covered by (1) an annual appropriation which has averaged approximately \$2.3 million annually over the last three years and (2) payments collected by the Department of Industrial Relations from insurance carriers in cases of industrial deaths where there are no surviving heirs. Revenues from these payments are approximately \$1.5 million annually. Subsequent injury payments are awarded by the Workers' Compensation Appeals Board (WCAB) and administered through the State Compensation Insurance Fund. The Attorney General represents the State's interests in the WCAB hearings.

The following table shows the Subsequent Injuries Fund outstanding liability as of December 31, 1977.

TABLE 2

*** UNAUDITED ***

WORKERS' COMPENSATION:
ESTIMATED OUTSTANDING LIABILITY*
AS OF DECEMBER 31, 1977
SUBSEQUENT INJURIES FUND

All open reported cases	\$ 33,481,000
IBNR: projection based on 1977 reporting	17,476,000
Re-opened: projection based on 1977 reporting	<u>28,000</u>
Subtotal	<u>\$ 50,985,000</u>
Administrative costs	
SCIF	\$ 2,549,000**
Attorney General	<u>3,929,000***</u>
TOTAL	<u><u>\$ 57,463,000</u></u>

* Rounded to nearest \$1,000.

** SCIF fee is 5 percent of benefits paid.

*** Attorney General charges are based on the average cost per closed case.

***UNAUDITED ***

Disaster Service Workers' Fund

The Disaster Service Workers' Fund provides for the payment of workers' compensation benefits to volunteer personnel who are injured while providing community disaster services. Program costs are covered by an annual appropriation which has averaged \$194,000 over the last three years. The program is managed by the Office of Emergency Services, and the SCIF adjusts claims and pays benefits.

The following table shows the Disaster Service Workers' Fund estimated outstanding liability as of December 31, 1977.

Honorable Richard Robinson
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TABLE 3

*** UNAUDITED ***

WORKERS' COMPENSATION:
ESTIMATED OUTSTANDING LIABILITY*
AS OF DECEMBER 31, 1977
DISASTER SERVICE WORKERS' FUND

All open reported cases	\$ 259,000
IBNR: projection based on 1977 reporting	11,000
Re-opened: projection based on 1977 reporting	<u>21,000</u>
Subtotal	<u>\$ 291,000</u>
Administrative costs	<u>\$ 36,000**</u>
TOTAL	<u><u>\$ 327,000</u></u>

* Rounded to nearest \$1,000.

** SCIF fee is 12 1/2 percent of benefits paid.

*** UNAUDITED ***

Uninsured Employers Fund

This fund provides for payment of workers' compensation benefits when an employer does not have compensation insurance and has not paid benefit awards to an employee as required by the Workers' Compensation Appeals Board. Funding is largely through an annual appropriation which has averaged \$4 million over the last three years. Penalties assessed against illegally uninsured employers are also deposited in the Uninsured Employers Fund. The fund is managed by the Uninsured Employers Fund Unit in the Division of Industrial Accidents, Department of Industrial Relations, which adjusts and pays the claims.

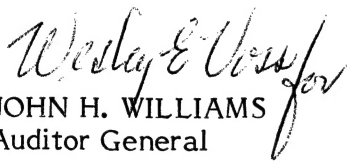
The estimated outstanding liability for reported claims as of December 31, 1977 was \$3,900,000. Since the fund is responsible for paying claims only when the employer has defaulted on the award, there is virtually no IBNR liability. Estimated administrative costs associated with the liability are \$800,000 annually. Recoveries from penalties are expected to be approximately \$500,000 annually.

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In-Home Supportive Services Program

Legislation passed in July 1978 made the State responsible for workers' compensation insurance for domestic employees working in homes of public assistance recipients. The Department of Social Services manages the program and may insure for the liability. However, if it does so, the Department will still be liable for benefits from January 1, 1978 to the effective date of the policy, since the legislation is retroactive to the beginning of calendar year 1978. The amount of the liability is unknown at this time.

Respectfully submitted,


JOHN H. WILLIAMS
Auditor General

Staff: Harold L. Turner, Audit Manager
Mary M. Quiett
Gerald A. Silva
Michael L. McGarity

Attachment: Response to the Auditor General's Report

STATE FUND

1275 MARKET STREET • SAN FRANCISCO, CALIFORNIA
TELEPHONE (415) 565-1234

November 2, 1978

Mr. John H. Williams
Auditor General
925 "L" Street, Suite 750
Sacramento, California 95814

Dear Mr. Williams:

The draft copy of Letter Report No. 726, "State Liability for Workers' Compensation", dated November 1978, has been reviewed by the State Fund.

We believe the report accurately reflects the State's uninsured workers' compensation liability as of December 31, 1977.

We appreciate the opportunity of reviewing the draft copy. We find no exceptions.

Sincerely,



President

EAS:ps

cc - Mr. Bob Denison, Manager
Governor's Safety and Rehabilitation Program